

March 10, 2014

Chairman Megna
Chairman Crisco

Committee Members:

I am Bill Kiley, President of Connecticut Underwriters, Inc. in Middletown and past President of the New England Surplus Lines Association. I am here on behalf of the Association and Connecticut Underwriters to oppose raised Bill 5366.

By mandating the inclusion of non-admitted insurer's or their representatives to comply with 38a-308, in essence takes away the ability of the Surplus Lines Market to operate how we were intended. The Surplus Lines Market is free of rate and forms so we can tailor policies for insured's who otherwise would not be able to obtain insurance. More specifically, Section 2(c) of the proposed bill will not allow for non-admitted insurers of homeowners to offer anything but "replacement cost with material other than like kind and quality."

Most, if not all non-admitted homeowner's policies are written on ISO Homeowner Forms. These un-endorsed forms would comply with the wording, however many forms are endorsed with a Functional Replacement Cost Form, also an ISO Form.

This form, which is included, states "'Functional replacement cost" means the amount which it would cost to repair or replace the damaged building with less costly common construction materials and methods which are functionally equivalent to obsolete, antique or custom construction materials and methods used in the original construction of the building." For example, if a home had plaster walls and was damaged by a covered peril, it would be replaced with drywall.

Legislating the proposed wording would have a dramatic negative impact to policyholders.

Functional Replacement Coverage is used when a functionally equivalent building can replace the original at a lower cost than would be required by an identical replacement.

Functional Replacement Valuation provides a lower valuation than Replacement Cost, resulting in a reduction of the amount of insurance coverage required and thus lower premiums.

Most Functional Replacement Coverage provisions provide that losses will be settled following one of these two methods:

- Replacement with less costly, but functional equivalent building, or in the case of a partial loss - restoration of the damaged portion in the same architectural style, but with less costly material (drywall).

The form also provides that the 80% building insurance requirement of these forms applies to Functional Replacement Cost, thereby reducing the amount of insurance required for full replacement and making the insurance more readily affordable for the owners of older homes, yet still making possible the full recovery of the cost to put the building back from damages, without requiring the insured to make expensive out-of-pocket costs to cover the substantial depreciation on an older home.

If Surplus Lines Brokers/non-admitted insurer's were required to only offer replacement cost with materials that are like kind and quality, we would have no other alternative but to require expensive appraisals of the homes.

This cost, passed to the consumer would be at least \$250. It would be necessary to do so in order that we insure the home to value. For example, if we were requested to insure a home built in 1940, valued at \$250,000 with plaster walls and ornate moldings with the Functional Replacement Cost Endorsement, the cost would be approximately \$875.

If we were required to offer terms without FRC we would have to appraise the home to determine its' true replacement cost.

If it was determined that the RC is \$400,000, because of the increase cost to repair or replace with like kind and quality, the cost to the consumer would be \$1,400, plus the cost of the appraisal. In both cases we are using the identical base rate.

As you can see, the proposed legislation takes away our ability to do what the non-admitted market was designed to do, tailor policies for insured's who are not eligible for the standard market.

THIS CHANGES THE POLICY. PLEASE READ
IT CAREFULLY.

FUNCTIONAL REPLACEMENT COST LOSS SETTLEMENT

FORM HO 00 02 AND HO 00 03 ONLY

SECTION I - CONDITIONS

The following definition is added when this endorsement is attached to the policy:

"Functional replacement cost" means the amount which it would cost to repair or replace the damaged building with less costly common construction materials and methods which are functionally equivalent to obsolete, antique or custom construction materials and methods used in the original construction of the building.

For the premium charged, Item **3.b. Loss Settlement** is deleted and replaced by the following:

b. Buildings under COVERAGE A or B:

(1) If, at the time of loss;

(a) The amount of insurance in this policy on the damaged building is 80% or more of the "functional replacement cost" of the building immediately before the loss; and

(b) You contract for repair or replacement of the damaged building for the same use within 180 days of the damage unless we and you otherwise agree;

we will pay, after application of deductible, the lesser of the following amounts:

(a) The limit of liability under this policy that applies to the building; or

(b) The necessary amount actually spent to repair or replace the damaged building on a "functional replacement cost" basis.

(2) If you do not make claim under Paragraph (1) above, we will pay, after application of deductible, the least of the following amounts:

(a) The limit of liability under this policy that applies to the building;

(b) The actual cash value of the damaged part of the building; or

(c) The amount which it would cost to repair or replace the damaged building on a "functional

replacement cost" basis.

(3) If, at the time of loss, the amount of insurance in this policy on the damaged building is less than 80% of the "functional replacement cost" of the building immediately before the loss, we will pay that proportion of the cost to repair or replace that part of the building damaged:

(a) After application of the deductible; and

(b) Without deduction for depreciation;

which the total amount of insurance in this policy on the damaged building bears to 80% of the "functional replacement cost" of the building, but not more than the limit of liability under this policy that applies to the building.

(4) To determine the amount of insurance required to equal 80% of the "functional replacement cost" of the building immediately before the loss, do not include the value of:

(a) Excavations, foundations, piers or any supports which are below the undersurface of the lowest basement floor;

(b) Those supports in **(a)** above which are below the surface of the ground inside the foundation walls, if there is no basement; and

(c) Underground flues, pipes, wiring and drains.

(5) If the actual cash value of the damage is less than the "functional replacement cost" then:

(a) We will pay no more than the actual cash value of the damage until replacement is complete. Once replacement is complete, we will settle the loss according to the provisions of **b.(1)** and **b.(3)** above.

However, if the cost to functionally repair the damage is both:

(i) Less than 5% of the amount of insurance in this policy on the building; and

(ii) Less than \$2,500;

we will settle the loss according to the provisions of

b.(1) and **b.(3)** above whether or not replacement is complete.

(b) You may disregard the "functional replacement cost" loss settlement provisions and make claim under this policy for loss or damage to buildings on an actual cash value basis.

You may then make claim for any additional liability according to the provisions of this Condition **3. Loss Settlement**, provided we are notified of your intent to do so within 180 days of the date of loss.

All other provisions of this policy apply.